INTERNAL AUDIT DEPARTMENT
2003 BUSINESS PLAN

COUNTY OF ORANGE
CALIFORNIA

February 7, 2003

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INTERNAL AUDIT DEPARTMENT
2003 BUSINESS PLAN

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EXECUTIVE SUMMARY

MISSION STATEMENT: The mission of the Internal Audit Department (IAD) is to provide highly reliable, independent, objective evaluations and business and financial advisory services to the Board of Supervisors and County management to assist them with their important business and financial decisions, and to protect and safeguard the County's resources and assets.

We support and assist the Board of Supervisors and County management in the realization of their specific business goals and objectives. Our contribution to this effort is testing and reporting on the effectiveness of their internal control systems and processes. County management relies on these systems and processes for safeguarding the County's assets and resources, for reasonable and prudent financial stewardship, for accurate recording and reporting, and for achieving the County's goals and objectives.

We are recognized for our expertise in assisting the County enhance its business processes while strengthening the protective internal control environment the public expects, relies upon, and demands. We are committed to a process of continuous learning and improvements within our department to keep updated on developing industry practices. Such constant renewal keeps the IAD and its staff professionally current, refreshed, invigorated, and responsive to the County's needs for attestation, compliance assurance, accountability testing, and business improvement by implementing best industry practices with regard to internal control and accounting systems and processes.

Internal Audit provides a variety of audit services to its primary client, the Board of Supervisors, who have the elected responsibility and accountability for the financial stewardship of the County. Another recipient of our audit services is County management who have the responsibility for day-to-day operation of the County departments and agencies. In addition, our published reports are used by various Federal and State regulatory agencies, the grand jury, the media, the investment community, and the public at large.

To meet our clients' expectations and for us to function effectively with reliability and credibility, the Internal Audit Department must ensure our reviews and assessments of County operations are independent, accurate, and unbiased. Therefore Internal Audit follows, when appropriate and necessary and depending on the type of audit being conducted, the exacting ethical and professional standards promulgated by the American Institute of Certified Public Accountants (AICPA), by the Institute of Internal Auditors (IIA), by the Information Systems Audit and Control Association (ISACA), and by the Government Accounting Office (GAO).

Internal Audit continues to implement for calendar year 2003 the two fundamental strategic goals begun in prior years and going back to the vision and formation of the department. These two goals remain at the heart of our operation. We reassess them annually and they continue to be relevant in guiding the professional direction of the Department.

1. We assist the Board of Supervisors and County management in ensuring the County's assets and resources are safeguarded, the County's accounting and financial reporting is timely and accurate, and the County's management has timely information and critical analysis for its business and economic decisions.

2. We provide professional assurance, attestation, and confidence to our clientele on the County's internal controls, accounting records, and financial and business operations through our published audit reports and reviews.

We incorporate these Business Plan goals into our annual Audit Plan. Our Audit Plan is submitted, discussed and approved at the beginning of each calendar year by the Audit Oversight Committee (AOC). We are dedicated to completing our annual Audit Plan while continuing to be flexible and responsive to the Board's requests for audit services whenever the need arises.

The Audit Plan has at its core the traditional audits of "hard-controls" such as segregation of duties, limiting access to cash, and accurate originating accounting entries and transactions. Examples of these traditional audits in our Audit Plan include our core business functions identified as Attestation Services and Mandated Audits (ASM), Departmental Control Reviews (DCR), and Information Technology Audits (IT). IT continues to focus on issues in the County's Comprehensive Accounting and Personnel System (CAPS). Our reports contain opinions regarding the status of internal controls or the County's compliance with grant or other governing provisions. Our reports also include recommendations to management regarding improvements to specific accounting processes and internal controls. Based on follow-up work performed on the status of our recommendations, we are proud to say (and also compliment our partnership with County management because they see value in our recommendations) that County management substantially implements our recommendations.

We combine these three core groups of "hard control" audits (ASM, DCR, and IT) with facilitated Control Self-Assessment (CSA) workshops to achieve the balanced audit coverage of the County we desire. The CSA workshops address the "soft control" aspects of a business operation such as, communications, ethics, and morale, and planning and risk assessment. In these workshops, we facilitate and attempt to discover if the work environment allows surfacing of business problems. The participants of the workshop and their management self-identify problems, issues, or concerns and ways they themselves can improve upon their own work environment. This process is an innovative and enlightened management approach to workplace problem resolution.

For the prior year 2002, we successfully met our two key outcome measures. Our audit efforts and the diligence of County management in managing its operations and addressing their control environments contributed to the achievement of these measures. Our two key outcome measures were successful last year because:

- **The County had no defalcation or reported cash loss exceeding $50,000.**
- **A high percentage of clients reported they received information and/or recommendations that were helpful to them in safeguarding the County's assets and making business decisions. With few exceptions, our control recommendations were addressed by management and implemented.**

MISSION & GOALS

A. Mission:

The mission of the Internal Audit Department is to provide reliable, independent, objective evaluations and business and financial advisory services to the Board of Supervisors and County management to assist them with their important business and financial decisions, and to protect and safeguard the County's resources and assets.

B. Goals:

Internal Audit continues to implement for calendar year 2003 the two fundamental strategic goals begun in prior years and going back to the vision and formation of the department. These two goals remain at the heart of our operation. We reassess them annually and they continue to be relevant in meeting the audit needs of the County.

1. We assist the Board of Supervisors and County management in ensuring the County's assets and resources are safeguarded, the County's accounting and financial reporting is timely and accurate, the County's management has timely information and critical analysis for its business and economic decisions.

2. We provide professional attestation, assurance and confidence to our clientele on the County's internal controls, accounting records, and its financial and business operations through our published audit reports and reviews.

C. Key Outcome Indicators:

Key Outcome Measure #1:

Department:	Internal Audit Department
What is it?	Defalcations of County resources.
Why is it important?	Defalcations bring bad publicity and weaken public confidence in County operations.
How are we doing?	The County did not have a defalcation or reported cash loss exceeding $50,000.

Key Outcome Measure #2:

Department:	Internal Audit Department
What is it?	Usefulness of reports and client satisfaction.
Why is it important?	Lets us know we are adding value.
How are we doing?	A high percentage of clients reported they received information that was helpful to them in safeguarding the County's assets and making business decisions. With few exceptions, our control recommendations were addressed by management and implemented. Additionally, Internal Audit is getting increasing requests for participation and/or advice on internal controls related to business reorganizations and financial system implementations.

D. Key Outcome Indicator Reporting:

We submit quarterly reports to the AOC reflecting cash loss activity and the results of follow-up audits we perform to verify that departments have implemented our suggested recommendations.

OPERATIONAL PLAN FOR EACH GOAL

Internal Audit Department's goals and Audit Plan constitute the operational plan for how we will function and what we will accomplish during the year 2003. The critical elements in the Audit Plan this year are the following commitments:

- We will accomplish all audits mandated by State law, as well as any audits required by contracts and grants. (These audits are included in the FAM category of audits.)

- We will provide regular assessments of critical business functions by conducting Control Self-Assessment workshops, Departmental Control Reviews, and Information Technology Audits and will factor the results into our annual analysis of our audit coverage of County operations.

- The IAD will contract with external sources for specialized audits, information technology, and other types of professional expertise to extend, complement and train our audit staff, or to provide an expertise we do not have internally.

Effective December 30, 1999, the Internal Audit Department implemented the Performance Incentive Program (PIP). The Management Performance Program (MPP) was also implemented shortly thereafter. All of our audit staff have attended the Enlightened Leadership classes.

The Internal Audit Department is fully supportive of PIP and MPP as County of Orange initiatives, and we are implementing them in a manner that conforms to the County of Orange's goals. Managers and Supervisors accomplish the human resource department directives by meeting with staff and our Director to address PIP and MPP goals and answer questions and concerns. Internal Audit feels this collaborative process will ensure that both the department's goals and objectives and individual goals are consistent. Labor Management Committee (LMC) is an active part of our management structure and two of our employees are represented on the LMC for Auditor-Controller/Internal Audit. One is a general unit member who is also a team leader and one is a management representative. The Spotlight Employee Recognition was implemented as well as the leadership phase of LEAD.

A. *Clients:*

The Internal Audit Department reports directly to the Board of Supervisors, our primary client. The Board of Supervisors has the elected responsibility and accountability for financial stewardship of the County. A sub-committee of the Board, the Audit Oversight Committee, provides executive oversight and guidance to the internal audit function. The membership of the committee currently includes the Chairman and Vice-Chairman of the Board of Supervisors, the Auditor-Controller, the Treasurer Tax-Collector, the County Executive Officer and two members from the private sector appointed by the Board. We meet, discuss, and report our progress on the Audit Plan to the AOC on a scheduled quarterly basis and more often if issues or events require it. In addition, the AOC is advised regarding the County's external auditing activities conducted by the independent and state and federal auditors.

There are proposed changes to the membership of the AOC that would reduce the seven members and meeting quorum by eliminating one public member and changing the Treasurer Tax-Collector to a non-voting ex-officio member. The Bylaws are currently under review by County Counsel prior to seeking final approval of the Board of Supervisors by December 31, 2002.

Another important recipient of our audit services is County management. County management has the sole obligation and responsibility for establishing and maintaining the County's systems of internal control. Our work provides County management with professional and independent feedback regarding their internal controls and how well these are working.

The support role internal auditing serves within any organization is expressed by these two paragraphs published in 1978 from the *Standards for Professional Practice of Internal Auditing*[1]:

> Internal auditing is an independent appraisal function established within an organization to examine and evaluate its activities. The objective of internal auditing is to assist members of the organization in the effective discharge of their responsibilities. To this end, internal auditing furnishes them with expert analyses, appraisals, recommendations, counsel, and information on the internal control aspects of the activities reviewed.
>
> The members of the organization assisted by internal auditing include those in management and the board of directors. Internal auditors owe a responsibility to both, providing them with information about the adequacy and effectiveness of the organization's system of internal control and the quality of performance.

The media reported many businesses have undergone incredible changes during the last few years of globalization, and we have also seen an increasing number of unbelievably large business bankruptcies. The media have also reported that these bankruptcies have caused tremendous harm to the public's confidence in business systems and operations and in their financial transactions. The investment and retirement portfolios of the public suffered losses in the trillions of dollars. The public questions the ethical conduct of our business leaders and the moral climate of business. However, during all this financial turmoil, the role of a well-run Internal Audit department remained constant. In remarkable contrast, it was reported that in companies where internal audit remained independent and where it was allowed to carry out its function, business operations continued successfully.

We in the County government environment are slightly different from typical commercial organizations, because County management has a public stewardship responsibility and our activities and reports have a concerned public audience both as recipients and participants in this process. An important element in our function (specifically provided by our reporting directly to the Board) is our organizational independence from the business functions we audit. Functional independence allows us to be forthright and candid in reporting findings and recommendations resulting from our audits. Our published reports are filed with the Clerk of the Board and are part of the public record in order to promote transparency.

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[1] *Standards for Professional Practice of Internal Auditing* (Altamonte Springs, FL: the Institute of Internal Auditors, 1978).

We follow rigid professional ethics and specific quality and performance standards in conducting our work. Consequently, any reader or user of our published reports is the recipient of a quality-assured product and is able to rely on our opinions and conclusions. The readers or users of our reports include County management, the general public, the media and news organizations, the investment community, third party grantors who use our audits for compliance assurance, and external auditors who use our reports to assess internal controls and financial statement risk.

B. Challenges:

No business environment is without challenges and the strength of an organization is its ability to meet challenges head on and develop appropriate strategies and solutions. Often, how we deal with challenges may impede progress toward achieving the goals and objectives set forth in the operational plan because we have to change priorities on how our resources are applied. However in our opinion, the IAD has enough strength and flexibility to achieve the majority of the goals and objectives put forth in the annual operational plan.

Two challenges seem to be constant for the Internal Audit Department each year.

I. The dynamic financial nature of the County, which includes managing the decreased revenues caused by state deficits, requires flexible audit plans and resource planning schedules. In addition, Internal Audit must be ready to respond to unscheduled assignments from the Board. We estimate the possible hours such reviews entail based on history and plan reserve hours specifically for this purpose. Occasionally these reviews take longer and absorb more hours than we reserved. When this occurs, we realign and supplement our resources as needed to include hiring temporary help and consultants. For the 2003 Audit Plan, we have reserved 1600 hours for Board requests for audit services.

II. Staff turnover and their replacement as well as the addition of new audit initiatives and responsibilities such as, Information Technology (IT) Audits (discussed below in IT issues) will challenge us and affect the completion of our annual audit plan. During 2002, we lost two of our senior auditors to higher paying positions in government. The addition of IT audits expanded our range of audit services and required two additional audit staff. The pace of technological advancement, and the benefits to be realized by implementing these advances to improve many County business operations is increasing at an accelerating speed. We received two additional staff positions to accomplish the added initiative, however due to State budget deficits we are unable at this time to fill the additional positions.

Information Technology (IT) issues

We developed a long-term, two tier plan to address our increased audit coverage. The first tier and our initial concentrated effort focused on specific issues and areas in the County's Comprehensive Accounting and Personnel System (CAPS). The second tier addresses the distributed computing taking place in County departments and agencies.

a) An upcoming major upgrade of CAPS will completely change how this financial software operates. Because of the importance and impact of CAPS to the County's fiscal operations, we are coordinating with the Auditor-Controller to determine how to best approach the upgrade. Our Audit Plan next year contains focused IT Audits in high-risk areas of CAPS identified by the Auditor-Controller. We and our consultant are currently performing a risk assessment review of the CAPS payroll system.

b) During 2002, we entered into a contract with a consultant to jointly conduct a readiness review of the CAPS upgrade project and a risk assessment of the current payroll process in CAPS. Payroll was identified by the Auditor-Controller as the system in CAPS which had the greatest concern for him. The report for the readiness assessment will make recommendations to assist in mitigating risks in this important implementation. The report on the payroll system will identify which aspects of the payroll process require further audit review.

Because our plan increases dramatically our IT efforts over the previous years in an effort to meet the increasing needs of the County as well as their expectations for consulting and assistance, we began to immediately train audit staff in IT Auditing and the IT skills necessary to accomplish such reviews. Our goal in the Internal Audit Department was to end the year with several of the staff certified as Certified Information System Auditors (CISA). We had 13 members of the staff sit in June 2002 for the CISA exam and 11 passed this rigorous exam. Two of the staff passing the exam submitted their application for CISA certification and expect to receive their certificates by year-end.

C. Resources:

Our Audit Plan is based on 20,400 direct audit hours to be provided by 14 audit staff. The audit hours for the Director and Deputy Director are not included in the above total and the time planned for the three Audit Managers is adjusted downward to allow them time for planning, mentoring,problem solving, and administrative management.

The 20,400 hours are allocated to the following audit areas:

Attestation Services and Mandates (ASM): **6,650**
Information Technology Audits (IT): **4,750**
Departmental Control Reviews (DCR): **4,700**
Facilitated Control Self-Assessment (CSA): **2,280**
Compliance Audits: **1,100**

The plan also allocates an additional 920 hours for audit activities such as staffing the fraud hotline, reviewing cash losses, and administering data collection of external audits.

Within the 20,400 hours, we reserved 1,470 hours to respond to Board requests for audit services. In addition to our direct hours, we contract out to industry experts some computer and business information technology audits and limited lease revenue reviews. We estimate that these consultants will provide 800 hours of work effort. The costs for the contracted reviews are reflected in our budget. Our budget for two fiscal years, 2001-02 and 2002-03 is detailed on the following page:

INTERNAL AUDIT DEPARTMENT

Financial Plan - Fiscal Year 2002-03

DESCRIPTION	OBJ	2001-02 Approved Budget	2002-03 Approved Budget
Salaries	0101	1,258,156	1,578,262
Overtime	0103	3,200	6,000
Vacation Payoff	0105	15,000	8,000
Performance Incentive Pay	0110	0	7,555
Other Pay	0111	624	828
Retirement	0200	27,791	140,666
Executive Def Comp Plan	0204	4,025	8,222
Unemploy. Ins.	0301	1,007	2,389
Salary Cont.	0305	4,763	6,822
Health Ins.	0306	93,986	145,973
Dental	0308	10,378	14,940
Life Insur.	0309	1,522	2,508
Accid. D & D	0310	281	420
Other Insur.	0319	1,433	4,368
Wrkr's Comp.	0352	3,132	4,176
Medicare	0401	17,315	21,251
TOTAL - Sal. & Ben.		1,442,613	1,952,380
Telephone	0701	20,000	22,300
Insurance	1100	5,229	3,977
Maint - Equip	1300	5,200	5,200
Maint - B & I	1402	10,000	23,000
Memberships	1600	1,920	2,710
Office Exp.	1800	86,511	75,200
Prof/Spec Svs.	1900	353,484	179,111
Pub./Legal Not.	2000	5,000	5,145
Rent/Lease - Eq.	2100	3,840	3,780
Rent/Lease - Bldgs. & Improv.	2,200	5,040	5,040
Spec. Dept Exp	2400	15,000	61,000
Trans & Travel	2600	9,000	11,560
Tran&Trav. - Mtgs	2700	46,100	54,200
TOTAL - Svs. & Suppl.		566,324	452,223
Equipment	4000	0	0
Intrafund Tfrs.	5100	(233,450)	(168,425)
TOTAL BUDGET UNIT		1,775,487	2,236,178
REVENUE:			
Intergovernmental			
Charges for Svs (7320)		86,450	128,022
Miscellaneous			
TOTAL - Revenues		86,450	128,022
NET COUNTY COST		1,689,037	2,108,156
POSITIONS		20	22

D. *Strategies to Accomplish Goals, Intermediate Targeted Outcome Indicators and Measures:*

Operational Strategies to Accomplish Our Goals: We support and assist County management and their business goals and objectives. Our contribution is testing and reporting on the effectiveness of their internal control systems and processes as these relate to safeguarding the County's assets and resources, prudent and reasonable financial stewardship, accurate recording and reporting, and achieving the County's goals and objectives.

The table below summarizes the professional activities we accomplish and areas we cover yearly. For more detail on the professional aspects of our function, please see the more detailed discussions in Section F, Caseload/Client Data, page 17. Because our activities are integrated into the yearly audit coverage provided, we cannot separate the activities and match them to either of the goals since our activities support both.

- Develop and perform an annual audit plan.
- Keep the Board of Supervisors, AOC, and County management informed of audit issues and results.
- Follow a recognized internal control framework (COSO).
- Follow professional standards.
- Encourage professional certifications for staff.
- Develop and train audit staff.
- Apply MPP and PIP.

STRATEGIES AND PLANS TO ACCOMPLISH GOALS	INTERMEDIATE TARGETED OUTCOMES AND MEASURES
Develop and perform an annual Audit Plan approved by the Audit Oversight Committee.	All audits and reviews will be completed by December 31. Any mandated/grant audits will be completed by the deadlines required by law or contract. Audit recommendations from DCRs and IT Audits will be selectively followed-up or resolved. This will be done within 12 months and until the recommendation is implemented.
Continually reassess and modify the Audit Plan for the County based upon the assessment of business importance and impact and the results of CSA sessions, DCR reviews, and IT audits. Direct audit resources to "high" importance rated departmental areas and CAPS systems.	After completion of the scheduled DCR reviews, CSA sessions, IT audits, departmental and CAPS systems importance and impact will be reassessed. The Audit Plan will be modified annually based on the data generated by these processes. The IAD will improve its importance and impact assessment with regard to the County's information and technology efforts. We will partner with the County's external auditor (Macias, Gini & Co.) in their assessment of IT issues, and also bring in IT consultants as the need arises.

STRATEGIES AND PLANS TO ACCOMPLISH GOALS	INTERMEDIATE TARGETED OUTCOMES AND MEASURES
Keep the Board informed of emerging issues as these come to the attention of the IAD, including those not specifically identified through the audit process.	Each member of the Board of Supervisors will be briefed on audit matters whenever appropriate, but not less than twice quarterly. All periodic Audit Oversight Committee meetings will be supported by the IAD including: (a) preparation of agendas, minutes, distribution of same and exhibits and documents beforehand, (b) submission of status reports of on-going audits for each meeting, (c) briefings as appropriate on audit issues and findings. We will ensure that departments report external audits that include significant findings, to the Audit Oversight Committee, pursuant to the AOC Administrative Procedure No. 2. IAD will compile the information gathered from the departments quarterly, and will follow-up on any significant findings and brief the AOC.
Provide information to the Board and County management regarding both the adequacy and integrity of key controls over their business systems.	All audit reports will be distributed to the Board Members, Grand Jury, AOC Members, and formally to the Clerk of the Board, pursuant to AOC Administrative Procedure No. 1.
Use the recognized COSO control model framework. (See page 17 for a description of COSO). Use the COBIT control framework for IT audits performed.	We have scheduled and anticipated performing 4,700 hours for DCRs and 4,750 for IT audits in 2003 that will address the traditional "hard" controls identified in the COSO framework. We have scheduled and anticipate performing 2,280 hours for CSA workshops in 2003 that will address the "soft" controls identified in the COSO framework.
Complete all audits and comply with the Standards for the Professional Practice of Internal Auditing required by Government Code 1236 and the Internal Auditing Standards promulgated by the Institute of Internal Auditors. Ensure all financial audits resulting in an opinion to conform to the audit standards of the American Institute of Certified Public Accountants.	Each audit assignment will be internally reviewed for compliance with the Institute of Internal Auditors standards and this review will be documented in the audit working papers (using a quality assurance checklist) for every audit completed during 2003. Every three years, IAD will undergo a peer review to obtain independent assurance of our compliance with the IIA standards. In 2001, we underwent a peer review that concluded we are substantially in compliance with the IIA standards. The next peer review will be scheduled for 2004.
Continue to encourage staff to obtain professional certifications.	At least two additional professional certifications will be achieved during 2003. The departmental goal is to achieve in addition, two more Certified Information Systems Audit certifications.

STRATEGIES AND PLANS TO ACCOMPLISH GOALS	INTERMEDIATE TARGETED OUTCOMES AND MEASURES
Provide training opportunities to staff for professional development and to meet certification requirements.	Each auditor will complete at least 40 hours of continuing professional education training. Core training needs on internal auditing will be identified and addressed. Departmental training will be provided in Information Technology skills necessary to conduct these reviews and certification as Certified Information Systems Auditors will be actively pursued.
Effectively implement, establish, promote and monitor the Performance Incentive Program (PIP) and the Management Performance Plan (MPP).	Managers and Supervisors will accomplish this by meeting with staff and our Director to address PIP and MPP goals and answer questions and concerns. Internal Audit feels this collaborative process will ensure that both the department's goals and objectives and individual goals are consistent.

APPENDICES

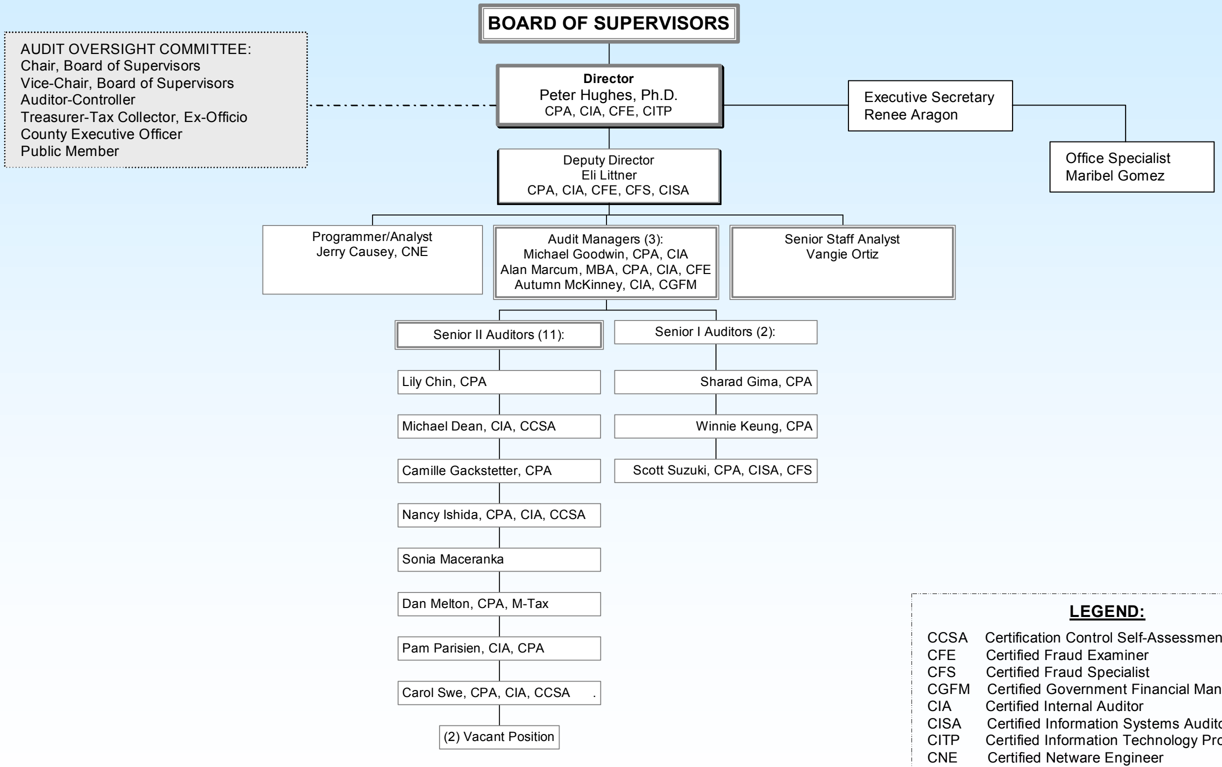
A. Organizational Chart:

County of Orange

Internal Audit Department

Organizational Chart

Business Plan 2003



BOARD OF SUPERVISORS

AUDIT OVERSIGHT COMMITTEE:
Chair, Board of Supervisors
Vice-Chair, Board of Supervisors
Auditor-Controller
Treasurer-Tax Collector, Ex-Officio
County Executive Officer
Public Member

Director
Peter Hughes, Ph.D.
CPA, CIA, CFE, CITP

Executive Secretary
Renee Aragon

Office Specialist
Maribel Gomez

Deputy Director
Eli Littner
CPA, CIA, CFE, CFS, CISA

Programmer/Analyst
Jerry Causey, CNE

Audit Managers (3):
Michael Goodwin, CPA, CIA
Alan Marcum, MBA, CPA, CIA, CFE
Autumn McKinney, CIA, CGFM

Senior Staff Analyst
Vangie Ortiz

Senior II Auditors (11):
- Lily Chin, CPA
- Michael Dean, CIA, CCSA
- Camille Gackstetter, CPA
- Nancy Ishida, CPA, CIA, CCSA
- Sonia Maceranka
- Dan Melton, CPA, M-Tax
- Pam Parisien, CIA, CPA
- Carol Swe, CPA, CIA, CCSA
- (2) Vacant Position

Senior I Auditors (2):
- Sharad Gima, CPA
- Winnie Keung, CPA
- Scott Suzuki, CPA, CISA, CFS

LEGEND:

CCSA	Certification Control Self-Assessment
CFE	Certified Fraud Examiner
CFS	Certified Fraud Specialist
CGFM	Certified Government Financial Manager
CIA	Certified Internal Auditor
CISA	Certified Information Systems Auditor
CITP	Certified Information Technology Professional
CNE	Certified Netware Engineer
CPA	Certified Public Accountant
M-Tax	Master's in Taxation

B. Management Team:

The Internal Audit Management Team consists of the following:

Director, Peter Hughes, Ph.D., CPA, CIA, CFE, CITP
Deputy Director, Eli Littner, CPA, CIA, CFE, CFS, CISA
Audit Manager, Michael Goodwin, CPA, CIA
Audit Manager, Alan Marcum, MBA, CPA, CIA, CFE
Audit Manager, Autumn McKinney, CIA, CGFM
Senior Staff Analyst, Vangie Ortiz

C. Labor Management Committee (LMC):

The Internal Audit LMC Members are as follows:

Senior Staff Analyst, Vangie Ortiz
Programmer/Analyst, Jerry Causey

D. Business Plan Team:

The Internal Audit Business Plan Team consists of the following:

Director, Peter Hughes, Ph.D., CPA, CIA, CFE, CITP
Deputy Director, Eli Littner, CPA, CIA, CFE, CFS, CISA
Audit Manager, Michael Goodwin, CPA, CIA
Audit Manager, Alan Marcum, MBA, CPA, CIA, CFE
Audit Manager, Autumn McKinney, CIA, CGFM
Senior Staff Analyst, Vangie Ortiz
Executive Secretary, Renee Aragon

E. Accomplishments:

CORE AUDIT ACTIVITY ACCOMPLISHMENTS

Department Control Reviews (DCR)
We completed all DCRs scheduled and budgeted in our 2002 Audit Plan. The DCRs focused primarily on internal control reviews of cash receipts and cash disbursements. Cash receipts DCRs are considered a core audit area due to the inherent risk that exists in cash handling, and the reviews are initiated in departments/agencies where a significant amount of monies are collected and processed. Cash disbursement DCRs included reviews of department/agency trust funds, special appropriation funds, and revolving funds to ensure monies were being used in accordance with their established purposes. One noteworthy DCR in 2002 was of the cash disbursements process at the Housing & Community Development Department (H/CD), where Internal Audit incorporated its new Information Technology (IT) audits initiative and reviewed controls and processes of H/CD's Section Eight Rental Assistance (SERA) information system, addressing system security and access issues.

Department Control Review Follow-Ups
The Follow-Up review process is necessary to ensure that the audit recommendations resulting from our DCRs are implemented satisfactorily. During 2002, Internal Audit implemented its "post follow-up" review process where we follow-up a second time with departments/agencies to ensure any audit recommendations that were not implemented in the initial follow-up audit have been fully implemented. Eight initial Follow-Ups and ten Post Follow-Ups were completed. The Follow-Ups were performed on DCRs completed in our CY 2000 and 2001 Audit Plans. In instances where all audit recommendations have not been fully implemented, the department/agency indicates its planned actions to implement the recommendations and Internal Audit performs a post follow–up review at a later date.

Attestation Services & Mandates (ASM)
We will complete by year-end all financial and mandated audits listed in the Audit Plan on schedule, except for the Annual Treasury Investment Compliance Review at 12/31/01. The Treasurer issued on October 21, 2002, a Request For Proposal (RFP) to outsource the Annual Treasury Investment Compliance Review for 12/31/01. We have completed the Treasury Funds Audits for quarters ending 12/31/01, 3/31/02, 6/30/02 and 9/30/02; and the Probation Audit for two years ending 6/30/01. We are in the process of completing the Treasury Funds Audit for quarter ending 9/30/02; the CAFR & Single Audit Assistance, the DA Auto Insurance Fraud Grant, the DA Workers' Compensation Fraud Grant, and the Tax Redemption Audit – three years ending 6/30/02. We will be starting the DA Spousal Abuser Prosecution Grant in November 2002 and will complete the audit by the end of December 2002.

Information Technology (IA) Audits
At the request of the Audit Oversight Committee (AOC), we added a new category of audits – Integrated Audits – to expand our range of audit services. IT Audits specifically focuses on issues in the County's Comprehensive Accounting and Personnel System (CAPS). To meet the AOC's request, we provided 2,640 hours of training to the audit staff to prepare them for the Certified Information Systems Auditor Exam. We had an extremely high pass rate of 80%, with eleven auditors passing the exam.

An upcoming major upgrade of CAPS will completely change the dynamics of how this financial software operates. During 2002, we entered into a contract with a consultant to conduct a readiness review of the CAPS upgrade project and a risk assessment of the current payroll process in CAPS. Both projects will be completed on schedule by December 31, 2002.

As a special feature within the IT audits, we implemented Computer-Assisted Auditing Techniques (CAATS) during 2002. We are using a proprietary software tool and have developed a toolset of computer-routines that will look for unusual data patterns in the individual data elements of the County's financial data on CAPS. During 2002, we developed several routines such as duplicate payment searches and employee vendor matches. Beginning in May 2002, we started issuing monthly reports of the CAAT results.

We were also requested by the Clerk-Recorder's Office to review their implementation of a back office upgrade to their automated cashiering system. This review will be completed on November 27, 2002

Control Self-Assessment (CSA)

We will complete all scheduled CSA workshops in our Audit Plan by December 31, 2002. We have completed the CSA workshops and are waiting to issue the final reports upon receipt of the action plans from the Community Services Agency, the Health Care Agency, and the District Attorney's Office.

ADDITIONAL AUDIT ACTIVITY ACCOMPLISHMENTS

Limited Reviews of Lease Revenue

These reviews are requested by PFRD and JWA and are performed on a fiscal year basis. We will complete ten scheduled limited reviews of lease revenue listed in the Audit Plan by December 31, 2002. Three additional reviews will be started and carried over to next year's Audit Plan. To help accomplish the reviews, we utilized audit staff from a local Certified Public Accounting (CPA) firm under an existing contract. We also utilized our own Internal Audit staff for the more complex reviews.

Technical Assistance to Others

We provided assistance to PFRD by facilitating certain financial and record keeping issues during the transition (ground lease to operating agreement) of three key operators in the Dana Point Harbor. We also assisted PFRD by reviewing the proposed lease assignments/amendments for Newport Dunes and Sunset Marina, focusing on the financial and record keeping clauses. Internal Audit also provided technical assistance to various departments, such as to the Clerk of the Board of Supervisors (revolving funds reconciliation process), to PFRD/Central Quality Assurance (contract administration), to PFRD/Real Estate Services (cash registers for certain park vendors), to CEO/Human Resources (prevailing wage reviews), and by having auditors participate in several RFP/contract evaluations and personnel interviews conducted by other County departments/agencies.

Cash Losses

We processed eighteen cash loss cases in 2002. Four cash losses met the criteria for field reviews by Internal Audit to determine the adequacy of internal controls and corrective actions. Most of the cash losses we processed involved the receipt of counterfeit bills received by County departments and the Justice Centers.

Board Requested Audits - Audit of Fund 14M

In May 2000, the Board of Supervisors directed Internal Audit to audit the expenditures of Fund 14M – Local Redevelopment Authority, which was established for the El Toro Master Development Program. This was an audit that involved a 100% review of $39 million dollars charged to the fund over a three-year period. The audit was completed and report issued in March 2002.

Fraud Hotline

We processed 23 Hotline incidents, 6 incidents were referred to County departments/agencies for investigation, 5 incidents were referred to the Welfare Fraud Hotline for investigations, 5 were referred to outside agencies, and 3 were "other," i.e., requests for information only, not enough information provided for investigation, etc. To date, only 1 of the 6 incidents referred to County departments/agencies for investigation remain open.

External Audit Activity

Each quarter, we compiled and presented a report of external audits in progress throughout the County to the Audit Oversight Committee, highlighting material findings.

Peer Review

During 2001, we successfully passed a Peer Review based on IIA standards and required by the Comptroller General of the United States in their published Government Auditing Standards. The Peer Review made several recommendations to improve our auditing and management processes. We have implemented the majority of recommendations. We have an outstanding recommendation regarding the revision of our Audit Department Charter that we are now working on for Board approval.

CPA and Other Professional Certifications

During 2002, we had two auditors from our staff submit their Form E (Experience) package to the State Board of Accounting to receive the Certified Public Accountant (CPA) credential. The experience packages were accepted and the CPA licenses were granted. Eleven auditors passed the Certified Information Systems Auditor (CISA) examination and two auditors met the experience requirements and received their CISA credentials. One auditor passed the Certified Internal Auditor (CIA) examination and received the CIA credential.

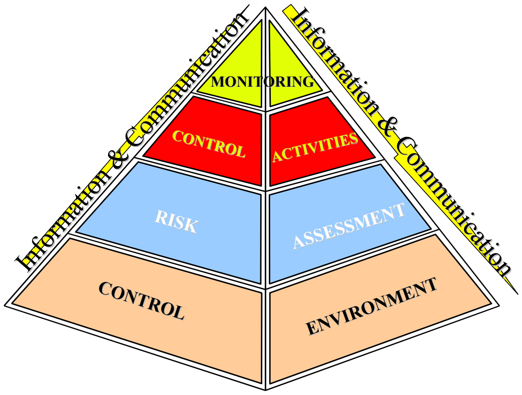
F. Caseload/Client Data:

Overview and Brief History of the Audit Department

The Internal Audit Department was established by Board Resolution 95-271, dated April 25, 1995, as a separate department independent from the County Auditor-Controller. Internal Audit's initial charge was to perform all audits required by Government Code Section 25250. This code section includes the biennial audits of County officers.

The County Auditor-Controller, as directed by the Board of Supervisors Resolution Numbers 69-733 and 82-162, previously performed these audits. In addition, the County Auditor-Controller elected to contract with the IAD to perform certain audits on his behalf. These audits include periodic audits of the Probation Department (Welfare and Institutions Code Section 275), and the quarterly verifications of assets in the County Treasury (Government Code Section 26923).

Auditing County Internal Controls Using a Standard Framework



Our audit role and services have been developed with the objective of providing balanced, uniform, and consistent coverage under the nationally recognized Committee of Sponsoring Organizations (COSO) control framework. This standardized framework provides definitions and responsibilities for internal controls. With this structure we can have meaningful descriptions, discussions, and analysis regarding an organization's internal control systems and processes. The internal control elements of the framework are depicted in the adjacent diagram. At the base of the diagram is the ***control environment***. The control environment includes "soft controls," which are the human factors such as morale and ethics that impact how well internal controls are implemented. It is the environment in which employees conduct their activities and carry out their individual control responsibilities, and it is the foundation for the control elements higher in the pyramid. Within the control environment, management ***assesses risks*** to the achievement of business goals. The ***control activities*** are the procedures that help mitigate risks and are traditionally prescribed to provide accountability, such as separation of duties, requiring approvals, reconciling assets and records, safeguarding assets and establishing audit trails. ***Monitoring*** refers to management's obligation to ensure that COSO elements are functioning as intended. Open lines of ***communication and business and accounting information*** are essential to ensure the successful operation of the activity or entity.

In addition to adherence with the COSO framework, Internal Audit must comply with certain professional standards that incorporate ethical and other audit performance requirements as explained below.

Ethical Requirements

Internal Audit strictly complies with professional ethical requirements. These include the ethical standards of the County and the rules of ethics promulgated by the American Institute of Certified Public Accountants (AICPA), the Institute of Internal Auditors (IIA), and the Information Systems Audit and Control Association (ISACA).

Professional Auditing Standards

Internal Audit complies with Section 1236 of the California Government Code, which states that all county employees who conduct internal audits ". . . shall utilize the general and specified standards . . . in the publication entitled Standards for the Professional Practice of Internal Auditing, published by the Institute of Internal Auditors, Inc." For audits that require an opinion on the fairness of financial statements, Internal Audit complies with generally accepted auditing standards and generally accepted accounting principles promulgated by the Financial Accounting Standards Board, and governmental generally accepted accounting principles promulgated by the Governmental Accounting Standards Board.

Sometimes laws, ordinances or state authorities specify the foregoing or other comparable standards with which we comply in the framework of the AICPA and IIA standards. Examples of such audits are the District Attorney Spousal Abuser Grant and the District Attorney Workers Compensation Fraud Grant that are conducted pursuant to "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions of the Comptroller General of the United States."